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Auditor General

February 17, 1987

P-523

Honorable Art Agnos, Chairman
Members, Joint Legislative
Audit Committee
State Capitol, Room 3151
Sacramento, California 95814

Dear Mr. Chairman and Members:

This letter updates our July 1985 report on the status of the Department of Transportation's (Caltrans) contract for the construction of the I-580 interchange in the Castro Valley. The I-580 contract was awarded on December 31, 1984, to Rail-Roadway Construction Company/R. A. Hatch Construction Company, a joint venture (joint venture). Since our July 1985 report, one subcontractor was decertified as a woman business enterprise, and another was decertified as a disadvantage business enterprise. In addition, the project has been delayed because the joint venture declared bankruptcy in November 1986 and Caltrans terminated the joint venture's control of the contract. As a result of this termination, the holders of the joint venture's performance bond, American Insurance Company and Fireman's Fund Insurance Company, assumed control of the contract in December 1986 and is to select a new contractor after February 16, 1987.

Decertification of Subcontractors

On July 15, 1985, we released a report entitled "Review of the Department of Transportation's Contract for the I-580 Interchange in Castro Valley" (P-523). In the report we concluded that the contract had been properly awarded. We found, however, that one of the subcontractors that Caltrans had certified as a woman business enterprise, H & H Electric, Incorporated, was ineligible for this certification, and we recommended that Caltrans decertify the firm. In its response to our report, Caltrans stated that the decision to decertify the firm was being postponed until the federal Department of Transportation concluded its investigation of the firm. On January 6, 1986, the federal Department of Transportation

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notified H and H Electric, Incorporated, that it was ineligible to participate as a woman business enterprise, and it notified C. E. Croff Construction, another joint venture subcontractor, that it was ineligible to participate as a disadvantaged business enterprise. Caltrans subsequently decertified the firms. Although, the decertification of these firms did not affect the status of the I-580 contract, neither of these two firms can participate as minority contractors in any Caltrans contracts.

Recent Contract Problems

According to the chief of Caltrans' Division of Facilities Construction, during the summer of 1986 subcontractors of the joint venture began contacting Caltrans and complaining that the joint venture was not paying them. Furthermore, rumors circulated that the joint venture was having financial problems and that one of the partners in the joint venture, R. A. Hatch Construction Company, was no longer participating in the construction project. According to Caltrans records, during the week of September 26, 1986, Caltrans noted that the workforce on the project had decreased significantly and that by October 20, 1986, work had ceased on a major element of the project.

On October 24, 1986, the joint venture asked for a three-month suspension of work due to financial problems. Caltrans denied the suspension requests twice, on November 7, 1986, and November 20, 1986. The last work performed on the project was November 13, 1986. On November 20, 1986, Caltrans notified the joint venture and the holders of its performance bond, American Insurance Company and Fireman's Fund Insurance Company, that the joint venture's control of work would be terminated in ten working days--on December 10, 1986--if work had not resumed. On November 26, 1986, the joint venture filed for reorganization under Chapter 11 of the U. S. Bankruptcy Code.

On December 23, 1986, Caltrans terminated the joint venture's control of the contract under Section 10253 of the Public Contract Code. According to the chief of the Division of Facilities Construction, the project is 36 percent complete, and approximately \$16 million of the \$44 million bid price has been paid.

Section 10221 of the Public Contract Code requires that all contracts have a performance bond and that, when control of the contract is terminated, the holder of the bond assumes responsibility for the performance of the contract. The American Insurance Company and Fireman's Fund Insurance Company, the joint venture's bonding companies or surety, issued a performance bond for \$22 million or half the bid price, at the time of the

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contract award. As a result, the surety will be liable for all costs, up to \$22 million, sustained above the contract bid price.

Section 10255 of the Public Contract Code allows the director of Caltrans to decide whether Caltrans will select a new contractor, complete the work itself, or direct the surety company to select a contractor to complete the contract. In this case, Caltrans has decided to allow the surety to select a new contractor. In this situation, Section 10256 of the Public Contract Code allows for an informal contracting procedure that does not mandate the usual state contracting requirements. The new contractor, however, must meet all state licensing and labor requirements.

To meet its responsibilities, the surety hired a consultant to prepare a bid package, which was completed on January 12, 1987. The consultant also selected the following list of prospective contractors:

Guy F. Atkinson Construction Company
Granite Construction Company
Dillingham Construction Company
S. J. Groves Construction Company
O. C. Jones Construction Company
C. C. Meyers Construction Company
Kiewit Pacific Construction Company
Piombo Construction Company
Steve P. Rados Construction Company
Gradeway Construction Company
Ghilotti Brothers Construction Company

Bids are due February 16, 1987, and it is anticipated that construction on the I-580 project will resume four to six weeks after the new contractor is selected.

Sincerely,


THOMAS W. HAYES
Auditor General